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AN OVER VIEW OF MUTUAL FUNDS IN INDIA

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ABSTRACT

Mutual fund is a financial organization, which collects the small savings from general public with the aim of investing it in the securities. The profit resulting from the investment is distributed among the contributors, who are called as unit holders. Mutual funds are based on the principle of "Trusteeship", which means working on behalf of someone else for the benefit of interested party and providing a protection to such party. In recent times, the concept of mutual funds gained momentum because of the increasing complexities of capital market. It is difficult for an individual investor to create and manage his portfolio of investment due to the lack of knowledge, expertise and experience about stock market. Mutual funds provide the benefit of diversification to unit holders as a result of which risk of investment gets minimized.

Present paper is a modest attempt to study the growth of mutual funds in India and to analyze the trends in sector-wise and scheme-wise resource mobilization by mutual fund industry. Secondary has been collected from various sources and analyzed by using appropriate statistical techniques.

KEY WORDS: Mutual Funds, Resource Mobilization, Net Asset Value, Unit Trust of India, Schemes, Sector, Growth.

MUTUAL FUND - PRELUDE

Mutual fund is a special type of institution that acts as an investment channel. It is a professionally managed investment organization that pools the money of many individual investors having similar investment objectives. The money thus collected is invested by the fund manager in different types of securities as shares, debentures, money market instruments and so on, depending upon the objective of the scheme. Income earned and capital appreciations thus realized by the schemes are distributed among its unit holders in proportion to the number of units owned by them Thus it endows the individual investors, with an opportunity to invest in a diversified, professionally managed portfolio at a relatively low cost.

A mutual fund is a single, large professionally managed investment organization that combines the funds of many individual investors having similar investment objectives. It designs its schemes to meet the needs of different types of investors in terms of nature of investments, dividend distribution, and liquidity, etc. the entire income/profits are distributed among the investors in proportion to their investments. However, expenses for managing the fund are charged to the fund. Mutual fund activity has come to play an important role in our development efforts.

Mutual Funds in India – Historical Perspective

Mutual fund industry has crossed about five decades in India. The Mutual Fund industry in India began in 1963 with the establishment of the Unit Trust of India (UTI) as an initiative of the Government of India and the Reserve Bank of India. Much later, in the year 1987, the first bank sponsored mutual fund State Bank of India Mutual Fund became the first non-UTI Mutual Fund in India.

Subsequently, with the introduction of new economic policy in 1991 the three pillars namely Liberalization, Privatization and Globalization paved the way for expansion. Year 1993 heralded a new era in the Mutual Fund industry. This was marked by the entry of private companies in the sector. After the securities and Exchange Board of India (SEBI) Act was passed in 1992, the SEBI Mutual Fund Regulations came into effect in 1996. Since then, the Mutual Fund companies have continued to grow exponentially with foreign institutions setting shops in India, through joint venture and acquisitions.

As the industry expanded, a non-profit organization, the Association of Mutual Fund in India (AMFI), was established on 1995. Its objective is to promote healthy and ethical marketing practices in the Indian Mutual Fund industry. SEBI has made AMFI certification mandatory for all those engaged in selling or marketing Mutual Fund products.

Objective of the study

The core objective of this paper is to examine the growth of Mutual fund industry in India. Studying the reasons for growth and advising suitable strategies to increase the business of mutual funds are the other objectives of the study.

Sources of Data

Secondary data has been used in the present study. Secondary data has been collected from the reports of AMFI, SEBI, Stock Exchanges, News Papers and Journals.

Period of Study

The study is about Growth Trend of Resource Mobilization by Mutual Fund Industry in India – A Study covers 5 years period (2013 - 2017)

Review of Literature

For years, both academics and practitioners have been continuously attempting to measure the investment performance of mutual funds. During early years, in finance, the only rate of return on an investment was considered as the indication of how well it has performed and the risk component was not well thought-out. Later, in the 1950's Markowitz (1952) and Tobin (1958) suggested a means to measure risk in terms of variability of returns, or variance. Another solution came in late 1960's by Treynor (1965), Sharpe (1966) and Jensen (1968) as Treynor index or ratio, Sharpe index or ratio, and Jensen's alpha respectively. These performance measures compare the returns of professionally managed portfolios to the return of some standard benchmark portfolios. While these traditional measures are very useful, they possess potential problems in addressing key factors in evaluating portfolio performance as how to identify the benchmark for comparision, accounting for the effects of market timing, and incorporating the consequence of transactions cost.

Roy and Deb (2004) examined the Indian mutual funds on the issue of performance persistence by using Fama and MacBeth (1973) methodology. They studied 133 open ended Indian mutual funds covering the period 1992–2003 and found that past fund performance predicts the future fund returns significantly. Among the studies conducted on performance persistence during late 2000's, Agudo and Magallon (2005) studied European equity funds in Spain during the period of July, 1994 to June, 2000 by using both parametric and non-parametric techniques. The parametric tests indicated scarce existence of persistence in the performance while non-parametric methodology revealed the existence of same. Bilson et al. (2005) analyzed Australian retail superannuation funds over a period from September, 1991 to June, 2000 and used raw returns, Sharpe ratio, single factor model and multi factor models by Carhart (1997) and Gruber (1996). They found no evidence of performance persistence over a one year period but the same was found over a three year period.

Agarwal (2011) in his study "Measuring Performance of Indian Mutual Funds" has pointed out that there has been incredible growth in the mutual fund industry in India and attracting huge investments from all corners domestic and foreign investors.

Usha Rekha (2012) wrote an article on "Growth of Indian Mutual Fund Industry – A Review". Has discussed about the history of mutual funds in India, the mutual fund industry started with the setting up of Unit Trust of India (UTI) in 1964, till the entry of first non UTI mutual fund by SBI in 1987 UTI enjoyed the monopoly. Public sector banks were allowed to operate mutual fund business in

1987. Subsequently Private players and Foreign players have entered into Mutual fund operations.

Data Analysis

Growth Trend of Mutual funds

With liberalization, the Indian Industrial sector wants cheaper funds to face global completion. Banking intermediaries today cannot afford to reduce their margins but the household sector demands better returns. All these factors have spawned the success of a new intermediary called mutual funds. The mutual fund industry in India, which is a little over three decade old, has undergone a sea change since the introduction of mutual fund regulations in 1993. It was in this year that private and foreign mutual funds started participating in the industry. Today, the industry consists of the Unit Trust of India, mutual funds sponsored by public sector banks, insurance corporations, and those set up by private and foreign funds.

Table:1 – Assets Under Management (AUMs) during February, 2016 – February, 2017

Sl. No	Period	No. of schemes	Assets Under Management Rs. in crores
1	March, 2013	1,294	7,01,443
2	March, 2014	1,638	8,25,240
3	March, 2015	1,822	10,82,757
4	March, 2016	2,420	12,32,824
5	March, 2017	2,281	17,54,619

Source: *www.amfiindia.com*

From the above table (Table:1) it can be found that very impressive growth is recorded in the mutual fund industry in India during the past five years. During the year 2013 (i.e. on 31-03-2013) the assets under management were Rs. 7,01,443 crores at the same time there were 1,294 schemes on offer. The assets under management increased to Rs. 8,25,240 crores in one year and the number of schemes increased to 1,638. As on 31st March, 2015 the assets under management soared to 10,82,757 crores and the schemes increased to 1,822. By 31st March 2016, the assets under management has been increased to 12,32,824 and 2420 schemes. There has been a significant growth during 2016 – 17 financial year. The total assets under management recorded as 17,54,619 crores where as the number of schemes decreased to 2,281.

Once if we analyze the above table, the assets under management were increased by 2.5 times within a period of 5 years.

Reasons for Growth

From the above table it is observed that there is significant growth in mutual fund industry during the past five years. The following are the factors which caused for the growth.

The MF industry has been growing at an impressive rate in terms of Asset Under Management (AUM) in the last few years. Currently, the industry's AUM is more than Rs 17 lakh crore in the year 2017. And, there are more than 2200 schemes - in equity and debt – available in the market. Still, the MFs have a long way to go. Only 3-4% of the Indian household savings go to the mutual fund kitty but it is as high as 60% in the US and other developed countries.

- **Small Unit Price:** One of the most important factors is the prices of mutual fund units. Units are available at very less prices like Rs. 10 per unit. A person / investor who cannot purchase the shares of the companies directly can invest in mutual funds. The people who could not access capital markets directly can be accessed with the same by purchasing units of mutual funds.

- **Private Sector Operations:** in India private mutual funds started operation from the year 1993 – 94. The result is increased assets under management. Till 1993 – 94 there was only public sector. The expansion has resulted in improved coverage network. Large number of organizations have come up with new schemes with attractive offers.

- **Substitute to Banks:** Schemes like Open- Ended are just like banks, where one can purchase at any time during the working days and can sell at any time during the working days. Like depositing in the bank and withdrawing from the bank. Here, the mutual funds are looking attractive in terms of return on investment. Being the funds managed by professionally qualified experts, they are offering attractive returns. At the same time the risk is low because of diversification strategy.

- **Bullish Stock Market:** The stock markets are reaching new heights. Investors are coming forward to invest more. Because of lacking of stock market knowledge, lower quantum of investments they are approaching mutual funds. Bullish stock market results in increase in value of NAVs of mutual funds.

- **Conducive Regulatory regime:** The regulatory framework is also favoring the growth of mutual funds. Authorities like SEBI (Securities and Exchange Board of India), Reserve Bank of India (RBI), Ministry of Finance and Ministry of Company affairs are taking corrective measures time to time to protect the interests of the investors. Corporate governance practices and the practice of independent directors in the board are boosting the confidence of investors.

- **Large variety of Products:** Earlier, prior to privatization only one Company was operating in India Unit Trust of India (UTI). Presently 30 companies are operating and they are offering a large variety of schemes for different investors. Each company is offering a variety of offers like open ended, closed ended, tax funds, growth funds, income funds, overseas funds etc. investor can choose any fund based on his preferences. This flexibility attracts variety of investors.

- **Greater Yields:** Compare to other investment avenues mutual funds are yielding better returns, approximately 17%. Whereas banks are offering only 10% - 13%. The most important feature of mutual fund is liquidity and profitability. It means the units can be sold whenever the unit holder want to sell just like a withdrawal from bank. Mutual fund products generally preferred by the investors due to their high returns compared to lower return on bank deposits and government securities. During the past couple of years the returns of mutual funds are higher than bank term deposit rates.

- **Cost of Investment:** Asset Management Companies charge investors towards professional fund management and regular operational costs. All these expenses charged to an investor are together known as the 'total expense ratio' (TER); it is an annual charge on Assets Under Management (AUM) in terms of percentage. According to the Securities and Exchange Board of India's (SEBI's) guidelines, TER needs to be lower as AUM increases. The net asset value (NAV) of a mutual fund scheme is net of all liabilities including TER, and hence a lower TER results in higher returns and vice versa. The fees charged for to the custodial, brokerage and other services is very low in case of mutual funds. A lower distribution cost is also ensured through online transactions. Mutual funds are a relatively less expensive mode of investment compared to other direct investments in capital markets. SEBI has already abolished entry loads (costs) for mutual fund investors who invest directly through the channels owned by asset management companies. In addition, because of their scale, mutual funds benefit from lower brokerage, custodial and other fees charged to them by the service providers thus making them more cost effective as compared with direct investing.

- **Tax advantages:** Tax benefits extended to the mutual fund investors investing in equity mutual fund schemes too have positive impact on the growth of the industry as well as attracting the middle income especially salaried class to this investment. Mutual funds are tax-efficient form of investment for a retail investor.

- **Flexibility:** Mutual funds in India offer wider flexibility by means of dividend reinvestment, systematic investment plans and systematic withdrawal plans. As these funds are available in relatively low priced units, they are also affordable to the small investors. These funds have the option of redeeming or withdrawing money at any point of time as per the convenience of investors. Easy entry and exit from this investment is another attractive feature of this Investment.

- **Liquidity:** Equity investors use the mutual fund liquidity ratio to measure the demand for shares and the bullishness or bearishness of portfolio managers. The mutual fund units can be easily sold and monetized by the investors as there is not much procedure involved in getting back the money; rather just the fund manager or agent has to be informed about redemption. In simple words, dealing with mutual funds is similar to savings account maintenance in the bank.

- **Risk reduction by diversification:** Diversification is one of the main reasons for investing in mutual funds. With regard to diversification, mutual funds help the investor in two ways. First, mutual fund allows an investor to diversify into many different stocks for a nominal investment. Diversification facilitates investors to reduce the risk of one particular stock or sector, second, it also allows for more potential reward by offering a broader exposure to various stocks and sectors. Diversification of a portfolio is amongst the primary tenets of portfolio structuring and it is a prerequisite to reduce the level of risk assumed by the portfolio holder. A fund must hold different securities belong to different variety of sectors. It is a well-known fact that fund diversification also reduces and spreads the risk factor of investors risks compared to investing in a single stock, bond, and other available instruments.

- **New Schemes/features:** The analysis of the industry suggests there is an increased emphasis on product innovation. Mutual funds offer a variety of schemes across asset classes to satisfy varying needs over an investor's lifetime. Even a small investor can afford to invest in equity and debt markets as the minimum investment amount in a scheme can be as low as Rs.500. A slew

of innovate schemes catering to different needs of investors have hit the market in recent times and have been received positively by investors. Innovative schemes like hybrid funds (fund for funds), children funds, and fixed maturity plans and new schemes such as exchange traded funds and commodity-based funds have contributed for the growth of mutual fund industry.

- **Investor friendly Administration:** Dealing with a Mutual Fund reduces paperwork and helps the investors from many problems such as bad deliveries, delayed payments and unnecessary follow up with brokers. In mutual fund, there is no administrative risk of share transfer, as many funds offer these services in their Demat trading accounts, which finally save investor's time.

- **Fairness /Transparency:** The Securities and Exchange Board of India (SEBI) has issued guidelines to mutual funds to bring in more transparency in their dealings with investors and agents, while allowing them to charge a fresh transaction fee. The performance of a mutual fund is reviewed by various publications and rating agencies, making it easy for investors to compare fund to another. As a unit holder, the investors are provided with regular updates, for example daily NAVs, as well as information on the fund's holdings and the fund manager's strategy.

Suggestions to Improve Further:

Though growth in terms of assets under management is impressive, Indian mutual fund industry is much behind in the global context. The size of mutual fund industry of United States of America is 17,235 Billion US $ (as on September, 2015) and number of schemes were 9,616. In Europe demographically small countries like Luxemburg, France and Germany have recorded a very good amount of assets under management.

Mutual Funds need to take proactive steps to collect more funds from the public. They need to follow the following strategies.

1. Distribution Network: Tap the untapped: The primary responsibilities of the government and regulators are to safeguard the interest of investors. The government of India should consider enacting a separate comprehensive mutual funds act and clearly spell out the rights, duties and obligations of the various constituents of mutual fund to provide a uniform regulatory framework and to create a level playing field for all the mutual funds in the industry including public and private sector mutual funds. Still in India majority of the towns and rural areas have not been covered by mutual funds. The mutual fund industry is losing the potential of gathering surplus amounts from rural people. As compared to other network like postal or insurance the mutual fund network is very weak. Organizations should concentrate more on the untapped area. They should concentrate more on Tier II and Tier II cities. Till now, mutual fund industry could attract very insignificant portion of the population of India. There is lot of scope to increase the business. The following are few suggestions:

In India, Asset Management Companies (AMCs) have variety of distribution channels. Prominent amongst them are: Direct channels; Banking channels; Retail channels.

In the direct channel, customers invest in the schemes directly through AMC. In majority cases, the company does not provide any investment advice, so these investors have to assess the options before investing. The fund companies provide several tools to investors who invest through this channel. This includes monthly a/c statement, processing of transaction, and maintenance of records. In this channel most investors can invest either through websites or receive information through telephonic services provided by the company. Approximately 10-20% of the total sales of an AMC come through this direct channel.

The banking channel: The large customer base of banks, in advanced countries, has played an important role in selling mutual fund units. In 1990's this channel has also opened up in India. All kinds of Banks operating in India, including public sector, private and foreign banks have established tie-up with various fund companies for providing distribution and servicing. The banking channel is likely to develop as the most vital distribution channel for fund companies there are several reasons for the same. Customers remain invested in banks for long periods of time and therefore banks maintain a relationship of trust with their customers. Customers rely on advice provided to them by bankers as they are always on the lookout for better investment avenues. An additional advantage that banks provide is that the concerned customer becomes a permanent contact of the banks and therefore can be reached during launch of (new fund offer) NFO or new schemes any time in the future

The retail channel: A customer can deal with directly with a broker or sub broker belonging to a distribution company, instead of taking trouble of dealing with several agents. Distribution companies sell the schemes of several fund houses simultaneously and brokerage is paid by the AMC whose funds they sell. The retail channel offers the benefits of specialist knowledge and established client contact and, therefore private fund houses are generally prefer this channel. Some of the major players in India in this in this channel are: Birla sunlife, IL&FS, Cholamandalam and Karvey etc.. The key factor for this channel to sell a company's fund used to be the brokerage paid. The banking and retail channel generally contribute to about 50-70% of the total Asset under Management (AUM)

2. Tie ups NGOs and Postal Department: To improve the network and reach of mutual funds they may take the help of Non Governmental Organizations by paying some commission. Another important avenue can be found in the form of postal department. In India postal department is having largest network, mutual fund organizations can make use of the infrastructure for establishing their office by paying commission. This will result in reduced cost of management.

3. Education Programmes: Mutual Fund industry should try to educate the investors about the advantages of mutual fund investment. Necessary steps may be initiated by AMFI in this regard. Awareness among the people results in increased business. It is the duty of the industry to convince the investors by explaining the merits of mutual fund investment. Workshops/seminars and interactions with the people will spread the information about the mutual funds.

Besides expanding the network, the industry needs to spend a lot of money on the investor education to create awareness. Damodaran has announced that the regulator will soon carry out a nationwide campaign with the help of two leading bourses – Bombay Stock Exchange (BSE) and National Stock Exchange (NSE) – to educate investors. But, the regulator and Association of Mutual Funds in India (AMFI) initiative itself is not enough in this direction.

Instead of looking at others, the fund houses need to allocate a certain percent of their budget on the investors' education to create a nationwide awareness among retail investors as even highly qualified professionals including engineers and doctors too need to equip themselves with financial literacy. The recently conducted Price Waterhouse Coopers (PWC) study on the mutual fund industry also suggested that the Association of Mutual Funds in India (AMFI) can also take a proactive step by requesting colleges and universities to introduce financial planning courses. Students can be educated about the basic factors responsible for the equity market movement along with the nature of financial schemes like MFs, insurance and bank schemes. India needs a large number of financial planners to guide investors about the financial services; especially MFs. AMFI can suggest academic centers to introduce courses specifically designed for financial planning. The bundling of MF schemes with other financial verticals like the insurance sector can be another option to attract investors. One or two fund houses have already started working in this direction.

4. Innovative Products: mutual fund organizations should be able to provide a large number of variety funds to suit the requirements of variety investor. There should be a fund to match the expectations of all types of investors. Few people may look for growth, few people may look for income, some may look for tax benefit, in this context there should be funds for growth orientation, income orientation and tax benefit etc.

5. SEBI exclusive wing with more powers: It has been witnessed that the industry owes its credibility and growth to the efficient and effective regulation by SEBI. Hence, the SEBI should be vested with more powers. There should be a separate wing to monitor the mutual fund sector. To improve the transparency, it can be suggested that as the industry grows, it will become more important to add auditors and inspectors to periodically verify the internal controls and operations of funds with on-site examinations apart from auditing the accounts and transactions. The Indian mutual fund industry in terms of regulatory frame work is on par with the most developed markets globally. The regulator, Securities and Exchange Board of India (SEBI), has consistently introduced several regulatory measures and amendments aimed at protecting the interests of the small investor that indicates the long term growth of the industry. Efforts should be made to implement the Prevention of Money Laundering (PMLA) Rules. Anti-Money Laundering (AML) and Combating Financing of Terrorism (CFT) should be taken care by monitoring the activities of various players such as investors, brokers and asset management companies.

6. User friendly technology: One of the key challenges would be to improve the use of technology for efficient and seamless investor transactions between all the stakeholders like the Fund House, Registrar and the Bankers. The Government should make the Paper Less Transactions its priority. This enhances the confidence levels of the investors in addition to reducing the transaction costs such as printing, postage etc.

Conclusion:

To sum up, the MF industry has lots of opportunities and challenges ahead. They can overcome these challenges only if they think from the retail investors' point of view, shedding the elitist bias by confining themselves only to the four metros. The industry should expand their operations throughout the nation. There is no doubt to say that the future of mutual fund industry in India is very bright.

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